Equity Research; ISA millionaires

COLLINS SARRI STATHAM INVESTMENTS

Research Report

Report Date

15th December 2022

Analyst

Ravi Lockyer MSc Llb ASCI
Collins Sarri Statham Investments Ltd

Key Risks to Price Target

Not applicable

Please note the risk warnings and disclaimers on the last page of this document.

How long does it take to become an ISA millionaire?

According to official data from HMRC and released via a FOI ("Freedom of Information") request from www.InvestingReviews.co.uk the UK as of June 2022 has some 2,010 millionaires with the average ISA millionaire account of c. £1.41m.

There are 60 ISA millionaires with over £3m with the average ISA value in this bracket c. £6.2m.

Pot	Investor numbers	Average market value
£1m-1,999,999	1870	£1,227,000
£2m-2,999,999	80	£2,366,000
£3m plus	60	£6,199,000

Source; HMRC June 2022

In 2022 total amounts held in UK ISAs are c. £2.8bn. This has accumulated since 1987, when Chancellor Nigel Lawson introduced PEPs the forerunner to ISAs. The PEP/ ISA idea is thought to have originated from the USA its 401k tax free accounts offer similar benefits, but Lawson also wanted an appropriate 'holding account' for investors holding shares in the UK privatizations that took place during the 1980s and 1990s.

About a decade ago, when online chatter first emerged of 'ISA millionaires', it was the considered opinion that 'Lady Luck' must have played a significant role in creating this rare investor breed. But the fact that over 2,000 people have now achieved the £1m milestone suggests this has less to do with Lady Luck, (though she is still involved!) but far more to do with investment approach and having the time, inclination and commitment to invest.

The virtues of 'lifetime investing' using tax free accounts was extolled in a best-selling book by Baron Lee of Trafford published in December 2013; *"How to make a million- Slowly: Guiding Principles from a Lifetime Investing"*.

Baron Lee (formerly Tony Lee MP) was the first reported UK ISA/ millionaire. To briefly summarize his highly nuanced approach, he partly attributed his good returns to his preference for investing in small/ medium sized family companies and companies where directors are heavily invested /incentivized by shares in the companies they run. Baron Lee was an avid reader of investment 'gossip', and a *Financial Times* columnist for over a decade, he attended AGM meetings, met directors of his investee companies and had a very sound understanding of those businesses. Baron Lee invested a total of £125k in PEP/ ISA subscriptions for over a decade.

Whilst neither endorsing nor denigrating Baron Lee's approach, it is an investment truism that any investor should understand their own approach to investing. If it works, and it did work for him, then it's a good idea to stick to a successful formula.

Given the fact that inward funding into ISA accounts is limited by the UK Budget, (the current annual allowance limit is £20k has been frozen since April 2018) the accumulation effect of tax free savings for long term investors has certainly been significant. A pound in a tax free ISA is worth more than a pound in your pocket.

What sort of investor has a shot at becoming an ISA millionaire? How is it achievable? What sort of financial and mental commitment is required and for how long? What are the variables?

What sort of investor is required?

The author finds himself conflicted in having been brought up, and hence influenced by, an age of financial prudence. This experience has some advantages and drawbacks! During the 1980s and most of the 1990s very high nominal interest rates meant there was a real opportunity cost to holding financial assets, such as a dedicated equity portfolio given the high returns on cash or cash equivalent assets and given the considerable pressures on financial reserves i.e. the need to fund property purchases and other expenditures. There was, and remains, considerable temptation to invest/ divest/ divert funds to other asset classes or other needs.

By the late 1990s an investment mania had taken hold, the 1998-2000 'dot-com boom' which was succeeded by a few years of weak/ negative returns, as overvaluations were ironed out. There were significant geopolitical tensions which were remedied by a period of low US interest rates and considerable laxity in financial regulation in the run up to the 2008/2009 crash. That seismic event led to another period of financial laxity, 'ZIRP' 'zero interest rate policies' and 'quantitative easing' or central bank manipulation of bond prices and asset prices more generally from 2009-2021. However 2022 has marked a return to pre-2009 conventional norms in that global interest rates have had to be normalized due to high global inflation.

Investors of a certain age have therefore seen numerous 'investing cycles' and undergone some learning curve transformation as a result. One lesson is to stay invested despite short term turmoil, another is to avoid drawing down on invested funds........too much.

But arguably what exists now is an age of financial imprudence where significant industries have grown up on the back of enabling people to delay and avoid being financially prudent. The lifetime mortgage industry is one example. Another is the crypto currency phenomenon which has 'corrupted' the investment process by creating unregulated bogus assets on shaky financial platforms.

The young investor these days is often a young mortgage free single person dabbling in cryptocurrencies and 'technology' shares is a far cry from Chancellor Lawson's 'Sid' investor buying BP. BT or BG shares and benefitting from tax free dividends. The Generation Z investor is often a temporary 'proxy' investor i.e. one whose objective is to put down a deposit on a home.

The ISA has also undergone changes and now cater for cash investors, property investors, and as a vehicle for children's assets. Traditionally ISAs catered for investors whose main priority was to obtain tax free returns.

The financial climate has also changed with the regulatory emphasis focused on providing investors with products that are suitable for them taking into account their age, circumstances and specific needs.

To some extent, the travails of capital markets, various speculative manias, the manipulations of governments and central banks, the emergence of dubious alternative assets or investment schemes, constitute short term investment 'noise'. 'Noise' tends to put off, divert or fluster investors wanting to tread a long term path. However the numbers make clear that it still takes time and financial commitment to get to a large tax free account.

But in my view, the sort of investor with a shot at getting to 7 figures, as a rule of thumb, still needs to be :-

i) relatively young (given the timeframe required) i.e. under 30
ii) gainfully employed (to enable the funding of both living expenses and ISA commitments)
iii) financially prudent – i.e. not allowing spending/ gambling patterns to imperil the ISA – i.e. not a gambler in crypto currencies or borrowing to invest.
iv) have some financial understanding or an interest in the subject
v) 'committed' to the ISA i.e. viewing it as a long term project and able to commit the time and effort as well

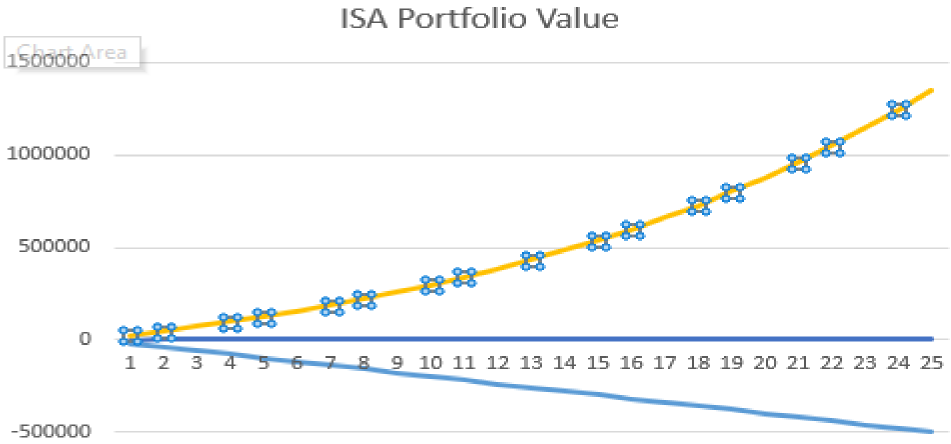
How long does it take?

Firstly if we assume:-

a) The ISA investor maxes out his/her investment subscription for as long as it takes for his/her ISA to reach £1m then we are looking at an extended period of 20-25 years of investment funding i.e. an investment of £400k - £500k.
b) The ISA investor has the right frame of mind to invest for 20+ yrs.
c) An annual portfolio return of 7% (capital and dividend are rolled up) – these returns are 'linear' i.e. at a constant rate p.a.
d) No withdrawals
e) No portfolio charges

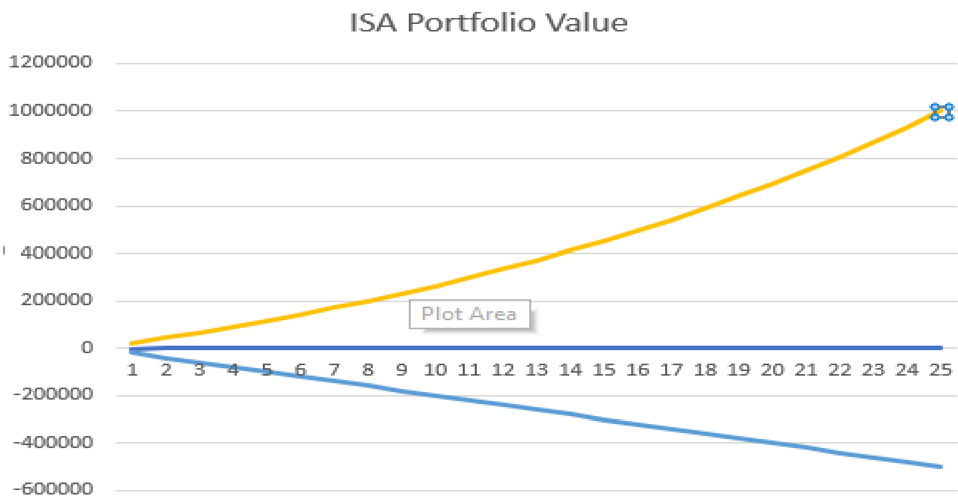
f) No changes in fiscal treatment of ISA account

According to our calculations, it takes 21.5 years to get to a £1m portfolio assuming a 7% return.



source:CSS investments Ltd

So let's change the return assumptions a bit, and **assume a 5% annual return. In this scenario an ISA with £500k (25 years) of invested capital would take 25 years to get to £1m value.**



source:CSS investments Ltd

Clearly the investment period has an inverse relationship with the investment return. A longer investment period is required if returns are lower.

The above data is good guidance of we assume linear returns. In recent years capital market returns have been non-linear and proved sensitive to shock events. It is fair to say that over 5 years returns have been very volatile. But haven't they always? Yes. Returns are smoothed out considerably over a 20 year – generation period.

The ISA in allowing tax free growth, i.e. not having to finance HMRC payments in respect of dividend income will create a very considerable pot of tax free income that can be used to supplement income if needed.

ANALYST CERTIFICATION:

The report's author certifies that this research report accurately states his personal views about the subject securities, which is reflected in the ratings as well as the substance of the reports.

RECOMMENDATIONS:

Collins Sarri Statham Investments Ltd (CSS) does not in any of its publications take into account any particular recipient's investment objectives, financial situation, and specific needs and demands. Therefore, all CSS publications are, unless otherwise specifically stated, intended for informational and/or marketing purposes only.CSS shall not be responsible for any loss arising from any investment based on a perceived recommendation.

No publication (including recommendations) shall be construed as a representation or warranty that the recipient will profit, nor avoid sustaining losses, from trading in accordance with a trading strategy set forth in a publication.

This research is non-independent and is classified as a Marketing Communication under FCA rules detailed in their Conduct of Business Rulebook (COBS). As such it has not been prepared in accordance with legal requirements designed to promote independence of investment research and it is not subject to the prohibition of dealing ahead of the dissemination of investment research outlined in COBS 12.2.18.

RISK WARNING:

Trading in the products and services offered by Collins Sarri Statham Investments Ltd (CSS) may, result in losses as well as profits as the value of investments may go down as well as up. You may not get back the full amount you have invested. Any reference to past performance should not be viewed as an indication of any future performance. Investments held in overseas markets are subject to the effects of changes in exchange rates which will impact on the value of the underlying investment. Leveraged products such as Contracts for Difference (CFDs), derivatives, commodities & Foreign Exchange (FX), carry a higher risk to your capital and they can lose their value rapidly.

SPECULATIVE TRADING IS NOT SUITABLE FOR ALL INVESTORS.

The information contained herein is based on materials and sources that we believe to be reliable however we make no representation or warranty, either express or implied, in relation to the accuracy, completeness or reliability of the information contained herein. Please note that the figures shown may, in some instances, be rounded to the nearest penny. Prices can move sharply from those quoted in this document. Current prices can be verified by calling one of our brokers. CSS is under no obligation to update the information contained herein. Neither CSS, nor its affiliates, nor its employees shall have any liability whatsoever for any indirect or consequential loss or damage arising from the use of this document.